PUBLIC UTILITIES COMMISSION
505 VAN NESS AVENUE
SAN FRANCISCO, CA 94102-3298

October 31, 2003

Agenda ID #2946
Ratesetting

TO: PARTIES OF RECORD IN APPLICATION 03-08-002

This is the draft decision of Administrative Law Judge (ALJ) Thomas. It will not appear on the Commission's agenda for at least 30 days after the date it is mailed. The Commission may act then, or it may postpone action until later.

When the Commission acts on the draft decision, it may adopt all or part of it as written, amend or modify it, or set it aside and prepare its own decision. Only when the Commission acts does the decision become binding on the parties.

Parties to the proceeding may file comments on the draft decision as provided in Article 19 of the Commission's "Rules of Practice and Procedure." These rules are accessible on the Commission's Website at http://www.cpuc.ca.gov. Pursuant to Rule 77.3 opening comments shall not exceed 15 pages. Finally, comments must be served separately on the ALJ and the Assigned Commissioner, and for that purpose I suggest hand delivery, overnight mail, or other expeditious method of service.

/s/ ANGELA K. MINKIN
Angela K. Minkin, Chief
Administrative Law Judge

ANG:hkr

Attachment

Decision **DRAFT DECISION OF ALJ THOMAS (Mailed 10/31/2003)**

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of PACIFIC GAS AND ELECTRIC COMPANY (U 39 M), a California Corporation, and THE COMMUNITY REDEVELOPMENT AGENCY OF THE CITY OF UNION CITY for an Order Authorizing the Sale and Conveyance of a Certain Parcel of Land in Alameda County Pursuant to Public Utilities Code Section 851.	Application 03-08-002 (Filed August 5, 2003)

OPINION GRANTING APPLICATION

Summary

We grant Pacific Gas and Electric Company's (PG&E) application pursuant to Pub. Util. Code § 851 to sell a parcel of land to the Community Redevelopment Agency of the City of Union City (Union City), California.[1] We find that adequate attention has been paid to the environmental effects of the sale and related demolition and site remediation work and that we need not do further analysis under the California Environmental Quality Act (CEQA). We determine that ratepayers and shareholders should each receive 50 percent of the gain on sale PG&E will realize upon conveyance of the property.

[1] The parcel at issue is identified in the purchase and sale agreement attached as Exhibit A to PG&E's application as "that certain parcel of real property located in the City of Union City, County of Alameda and State of California, identified by the Alameda County Assessor as Assessor's Parcel Map 087-0019-004-02 [and] the State Board of Equalization as . . . SBE No. 135-1-346-1."

Background

A. The Property

PG&E asks us to approve a sale and conveyance of a parcel of land located in Alameda County, California to Union City. PG&E bought the property in 1952 for $176,734, and is selling the property for $18,076,000.

Union City will use the 28.3-acre parcel (and an adjoining parcel) for a redevelopment project that will include affordable housing, office development, a BART[2] transit hub, pedestrian walkways, and other community amenities. PG&E once used the property to house a natural gas pipe wrapping and storage facility. In 2002, it ceased use of the property and states that the property is no longer used by or useful to PG&E.

The property contains underground and aboveground electric distribution lines and underground natural gas pipelines and valves. It contains a warehouse building that PG&E has agreed to remove. PG&E also will remove the distribution lines serving the warehouse and the underground natural gas pipelines and valves, and will relocate three underground electric distribution lines. PG&E will retain easements for use of the distribution lines that will continue to be necessary for its provision of electric service. It has determined that these easements will allow it to retain all rights necessary for current maintenance and future operation of existing facilities, including the right to enter onto the property for maintenance purposes.

The property and the adjacent parcel have also been the subject of environmental remediation. The adjacent parcel, formerly owned by Pacific States Steel, was the subject of a federal district court clean-up plan and other

[2] Bay Area Rapid Transit.

litigation. Part of the court-approved plan is Union City's commitment to construct a major new street running through the PG&E property and connecting an adjacent road, Decoto Road, to the Pacific States Steel site.

The PG&E property will also be remediated. PG&E has agreed to participate in a clean-up project implemented by the California Department of Toxic Substances Control. PG&E has commenced remediation of the property, and will leave $1.5 million in escrow upon the sale of the property to complete the remediation work.

B. Gain on Sale and Related Accounting Issues

PG&E calculates the gain on sale pre-tax at $16,310,641 and the after-tax gain at $9,664,707.[3] PG&E claims shareholders should receive this entire gain. It explains that the property consists of nondepreciable land, that ratepayers did not contribute to the initial acquisition of the property, and that PG&E has not recovered the purchase cost from ratepayers through depreciation.

PG&E asks that we either determine here that the gain on sale should accrue in its entirety to PG&E's shareholders, or that we defer the issue to the generic rulemaking on gain on sale issues that the Commission has indicated it will institute late in 2003.[4]

---

[3] PG&E also explains that the property consists only of non-depreciable land whose net book value ($176,734) will be removed from rate base upon Commission approval and close of the sale. Based on annual property taxes of $80,875, no annual operations and maintenance expense, and the Company's 2003 authorized cost of capital for distribution assets (11.22% on equity, 9.24% on rate base), PG&E estimates the 2003 revenue requirement for the property, including taxes, franchise requirements and provision for uncollectible accounts, to be $105,215.

[4] PG&E cites Decision (D.) 03-04-032, *mimeo.* at 21, n.5.

The Commission's Office of Ratepayer Advocates (ORA), the only party to protest the application,[5] opposes deferral of the gain on sale issue and instead urges us to find that all gains from the sale be allocated to ratepayers. It does not otherwise oppose the application. In an October 3, 2003 filing, ORA explained that ratepayers would suffer a hardship if this proceeding were bifurcated to defer the gain on sale issue because their just remedy would be deferred.

Discussion

A. Section 851 Analysis

The basic task of the Commission in a Section 851 proceeding is to determine whether the transaction serves the public interest: "The public interest is served when utility property is used for other productive purposes without interfering with the utility's operation or affecting service to utility customers."[6]

We have reviewed the proposed agreement to sell the property to Union City and find it does not impair PG&E's ability to provide utility service to the public. PG&E will retain proper easements in order to maintain distribution plant that will remain on the property. It no longer needs the rest of the property, as it has discontinued the natural gas pipe wrapping and storage activities the site once housed.

The property will be cleaned up as a result of the sale, which also affords public benefits. Moreover, the use to which the property will be put will provide

[5] Union City filed a motion asking us to defer the gain on sale issue and we received several letters expressing support for deferral so that we might allow PG&E to conclude the sale, and Union City to proceed with its project, as soon as possible.

[6] D.02-01-058.

positive community benefits in Union City. While this latter benefit does not help ratepayers directly, it does help establish that sale of the property benefits the public interest.

We therefore find that the sale meets the requirements of Section 851.

B. Environmental Review

CEQA[7] applies to discretionary projects to be carried out or approved by public agencies. A basic purpose of CEQA is to "inform governmental decision-makers and the public about the potential significant environmental effects of the proposed activities."[8]

Because the Commission must issue a discretionary decision (*i.e.*, grant Section 851 authority) without which the proposed activity cannot proceed, and because the activity has the potential to result in either a direct physical change in the environment or a reasonably foreseeable indirect physical change in the environment,[9] the application is subject to CEQA and the Commission must act as either a Lead or Responsible Agency under CEQA.

The Lead Agency is the public agency with the greatest responsibility for supervising or approving the project as a whole.[10] A Responsible Agency is required to consider the environmental consequences of a project that is subject to its discretionary approval, and in particular to consider the Lead Agency's

---

[7] Public Resources Code Sections 21000, *et seq.*

[8] Title 14 of the California Code of Regulations, hereinafter CEQA Guidelines, Section 15002.

[9] CEQA Guideline § 15378.

[10] *Id.*, § 15051(b).

environmental documents and findings before acting upon or approving a project.[11]

Union City's Redevelopment Agency (Agency) and the city council of Union City (City Council) prepared a proposal and conducted an environmental review that would (a) amend the City's 1988 Redevelopment Plan (Plan) to create an expanded project area, (b) change certain 1988 Plan time and financial limits, and (c) revise the list of proposed redevelopment programs and activities.

On September 24, 2001, the City Council and the Agency forwarded a Draft Environmental Impact Report (DEIR) to the State Clearinghouse (SCH #2000112010) and published the Notice of Availability in a local newspaper of wide circulation. The DEIR analyzed the proposed revisions to the Plan at a programmatic level, except for the five specific sub-projects proposed consistent with the original and revised Plan, which were also analyzed on a project level. Of the five projects, the proposed project subject to Section 851 review before the Commission is identified as "Specific Project 5: Intermodal Station District and Transit Facility Plan." On October 22, 2001, the City Council solicited oral comments on the DEIR at a public workshop during the 45-day public comment period.

A Final Environmental Impact Report (FEIR) was prepared and made available on January 17, 2002, formally addressing all comments received on the DEIR. Throughout the process, the City Council sought to develop alternatives that would mitigate the impacts of the project to the greatest extent possible. The FEIR incorporates both resource impact mitigation measures and a monitoring program designed to reduce impacts to a less-than-significant level in a number

[11] *Id.*, § 15050(b).

of areas, including Land Use, Hydrology and Water Quality, Aesthetics, Biological Resources, Geology, Cultural Resources, and Public Facilities.

At the same time, the FEIR acknowledges that there are three areas where impacts cannot be mitigated to a less-than-significant level, including the cumulative effect of land developments on regional air quality (impact IMAQ-2); the exposure of noise sensitive land uses near the project site to construction noise (impact NOI-3 and NOI-2); and contribution by the project to degraded level of service on arterial roadways (impact TC-2 and IMTC-1).

On February 26, 2002, the City Council and the Agency held a joint public hearing on the amended plan. On March 12, 2002, the City Council adopted the Findings of Fact, including applicable Mitigation Measures, the Mitigation Monitoring and Reporting Program and a Statement of Overriding Considerations (Resolution No. 249-02, Exhibit A). A Notice of Determination was subsequently filed with the state Office of Planning and Research, in compliance with Sections 21108 and 21152 of the Public Resources Code.

We have reviewed and considered the DEIR, the FEIR, and the discretionary decision by the City Council, and find that these documents are adequate for our decision-making purposes under CEQA. We conclude that there is substantial evidence that none of the proposed alternative sites would avoid or substantially lessen any potential direct, indirect, or cumulative significant impacts of the project and that the alternative analysis complies with the requirements of the Warren-Alquist Act and CEQA. We find that the City Council reasonably concluded that the proposed project, including the mitigation measures in the FEIR, is feasible and will avoid and/or reduce the majority of potential environmental impacts to less-than-significant levels.

Certain mitigation measures, as described in the FEIR, would lessen but not necessarily eliminate the potential adverse environmental effects associated

with the project and that those impacts remain significant and unavoidable. These impacts were in the resource areas of Air Quality, Noise, Traffic, and Circulation.

We conclude that the City Council reasonably found that there were no other feasible mitigation measures or alternatives that the City Council could adopt which would reduce these impacts to less-than-significant levels. We conclude that the City Council reasonably found that to the extent that these impacts could not be substantially lessened or eliminated, specific economic, legal, social, technological, or other considerations and project benefits identified in the Statement of Overriding Considerations supported approval of the project, including providing for a balance of development options, economic growth, and quality of life benefits.

C. Gain on Sale

We find that ratepayers and shareholders should each receive 50 percent of the gain from the sale of the property.

ORA claims that Commission precedent dictates that the gain on sale from this transaction be allocated between shareholders and ratepayers based upon the time the property was in rate base.[12] According to ORA, it is a fundamental tenet of economic theory that those who bear the burden be rewarded with the gain.

PG&E claims that the decisions ORA cites, D.89-12-057 and D.87-12-067, do not support ORA's position. PG&E also claims that D.94-01-028, in which the Commission allocated to shareholders the gain on the sale of land, governs here.

---

[12] ORA cites D.89-12-057, 34 CPUC 2d 199 (1989), and D.87-12-067, 27 CPUC 2d 1 (1987).

We have traditionally left consideration of the proper allocation of gain on sale to a case-by-case determination. In 1985, we allowed PG&E to sell a portion of its distribution system to the City of Redding (D.85-11-018, known as *Redding I*). We allocated the gain from this sale to ratepayers primarily because the ratepayers bore the risk of the investment.[13] As we explained in that decision,

> Risk analysis requires a case-by-case assessment of whether it was ratepayers or shareholders that bore the risks of investment. That inquiry is one of facts and facts will differ from sale to sale.

In *Redding II*, we reversed the *Redding I* holding, and found that allocation of the gain depended not on who had borne the risk, but rather on whether ratepayers had contributed any capital to the assets being sold or encumbered and on whether the transfer of assets harmed ratepayers.[14]

However, it at least one post-*Redding II* case, we stated that the risk-sharing approach of *Redding I* was the appropriate test for allocating the gain on sale. In developing a new manner of allocating the gain, we stated the following:

> We recognize that this policy is a departure from *the risk-sharing approach we have used in many previous gain on sale decisions*. However, both the risk-sharing policy and this new policy share a common objective, that of assuring that ratepayers continue to receive a fair and appropriate share of the capital gain yielded from the sale of an asset that must be replaced in utility service.[15]

---

[13] D.85-11-018, 19 CPUC 2d 161 (1985), 1985 Cal. PUC LEXIS 958.

[14] D.89-07-016, 32 CPUC 2d 233 (1985), 1989 Cal. PUC LEXIS 587.

[15] D.90-04-028, 36 CPUC 2d 235 (1990), 1990 Cal. PUC LEXIS 200, at *45-46.

Thus, it is presently unclear the extent to which the risk-allocation test of *Redding I* or the contribution of capital/ratepayer harm test of *Redding II* represent current Commission policy. For this reason, we have recently deferred many cases raising the gain on sale issue to our promised rulemaking on gain on sale issues, and PG&E asks us to follow suit here.

We do not believe deferral is warranted in this case. Regardless of the applicable test, we believe that ratepayers and shareholders should share the benefits from the sale of the property. We discuss our reasoning below.

In one of the cases ORA cites, D.89-12-057, the Commission adopted the proposal of ORA's predecessor, the Division of Ratepayer Advocates (DRA) to allocate the gain on sale to ratepayers. PG&E points out that we did so because PG&E had failed to make a timely showing in support of its own proposed ratemaking treatment.[16] Nonetheless, had the Commission believed the gain on sale treatment DRA proposed was manifestly unjust, we cannot imagine it would have chosen it. Thus, D.89-12-057 supports allocation of the entire gain to ratepayers.

PG&E also questions the applicability of the other case ORA cites, D.87-12-067. There, once again, as PG&E concedes the Commission allocated the proceeds from the sale of real property to ratepayers. While PG&E questions whether the Commission was motivated by a reason other than the merits of the issue,[17] it is undisputed that the Commission applied the gain on sale test

---

[16] 34 CPUC 2d 199, 283 (1989).

[17] "It is unclear to what extent the Commission's decision in D.87-12-067 regarding the gain-on-sale was punitive in nature." *Reply of [PG&E] to the Protest of [ORA],* filed Sept. 18, 2003, at 3.

advocated by ORA. Thus, once again, precedent supports allocating the gain to ratepayers.

In PG&E's cited case, D.94-01-028, the Commission allocated the entire gain to shareholders. However, the Commission explicitly limited the scope of the decision to circumstances not present here. We stated there that,

> This decision should not be regarded as precedent for other gain-on-sale cases. It is limited to the facts of this case, *where rate base property is sold under threat of condemnation and where the utility use to which the property had been put continues unchanged after the sale*.[18]

The property at issue here was not sold under threat of condemnation, and the property will no longer be put to utility use after the sale. Thus, D.94-01-028 is not binding here, but it does indicate that at least in one land sale situation, the Commission has found that shareholders should benefit from the gain on sale.

In a recent case with facts almost identical to this one,[19] we articulated at least two principles that the Commission should consider in determining how to allocate the gain on sale when the utility sells land that is no longer used or useful to a private entity.

> As a general proposition, whether property was in ratebase at the time of its sale should not determine by itself how net proceeds are allocated between ratepayers and shareholders. (Citation omitted.)

---

[18] D.94-01-028, 53 CPUC 2d 45 (1994), 1994 Cal. PUC LEXIS 45, conclusion of law 1 (emphasis added).

[19] The case involved a sale by PG&E of a parcel of land to the City and County of San Francisco that had previously been used to store natural gas. There, as here, PG&E dismantled the gas facilities, but maintained easements in order to have access to electrical lines running along the property's edge. There, as here, the property was no longer used or useful to PG&E, and would be used by the purchasing City for non-utility purposes (in the San Francisco case, for storage and parking; *see* D.02-04-005).

> A more important consideration is whether the property was ever in ratebase. (Citation omitted.) Also pertinent to the allocation of net proceeds is the extent to which ratepayers and shareholders benefited from any revenue generated by the property while surplus to the utility's regulated operations.[20]

While we deferred the issue of proper allocation of the gain on sale to our promised generic proceeding on the issue, we see no reason to do so here based on the foregoing precedent.

It is undisputed that the property at issue here has been in rate base. In its application, PG&E states that the "net book value ($176,734.00) will be removed from rate base (reduction to rate base) upon Commission approval and close of the sale."[21] In order to be "removed from rate base," the property must now be in rate base, so at least one criterion for allocation to ratepayers is satisfied.

Moreover, under either the *Redding I* or the *Redding II* tests, ratepayers should receive at least a portion of the gain on sale. There is no indication that PG&E's investment in the land it is now selling was a risk to the shareholders. The *Redding I* risk assessment test is designed to reward shareholders if they make investments in risky or speculative ventures because they also bear the burden of loss in making such investment decisions. Here, there is no indication that the land PG&E purchased in the early 1950s was part of any investment strategy for which shareholders took risks. Rather, PG&E used the property for natural gas services—a regulated function. Nor is there any need to provide PG&E's shareholders incentives in the future to invest in land. Land ownership is not part of PG&E's business; rather, PG&E holds land in order to house its

---

[20] D.02-09-024, 2002 Cal. PUC LEXIS 546, at *7.

[21] Application at 11.

regulatory functions. Nor has California real estate been a risky investment in past decades. Thus, the risk assessment test dictates that ratepayers be awarded at least part of the gain.

Under the *Redding II* test, ratepayers also deserve to share in the gain. While they will not suffer harm from the sale, since the property is no longer used or useful (one part of the *Redding II* test), they did contribute capital to purchase the land since the land has been in rate base.

We acknowledge that none of the foregoing tests gives us a clear indication of how precisely to allocate the gain. ORA seeks only a proportionate share of the gain for ratepayers, and not the entirety of the gain, while PG&E seeks the entire gain for shareholders. We believe the most equitable result in this case is to split the gain 50-50 between ratepayers and shareholders. This decision is based on the facts of this case and does not establish a general rule for allocation of the gain on sale in land sale cases. It may be that other, similar cases arise before we open our generic rulemaking. Those cases should be determined on their merits, without reliance on this decision, so that we can leave establishment of a general, precedential rule to our upcoming gain on sale rulemaking.

Assignment of Proceeding

Geoffrey F. Brown is the Assigned Commissioner and Sarah R. Thomas is the assigned Administrative Law Judge (ALJ) in this proceeding.

Comments on Draft Decision

The draft decision of the ALJ in this matter was mailed to the parties in accordance with Pub. Util. Code § 311(g)(1) and Rule 77.7 of the Rules of Practice and Procedure. Comments were filed on _____, and reply comments were filed on _____.

Findings of Fact

1. PG&E bought the property in 1952 for $176,734, and is selling the property for $18,076,000.

2. Union City will use the 28.3-acre parcel (and an adjoining parcel) for a redevelopment project that will include affordable housing, office development, a BART transit hub, pedestrian walkways, and other community amenities. PG&E once used the property to house a natural gas pipe wrapping and storage facility.

3. In 2002, PG&E ceased use of the property.

4. PG&E will retain easements over the property for use of the distribution lines that will continue to be necessary for its provision of electric service. The easements will allow PG&E to retain all rights necessary for current maintenance and future operation of existing facilities, including the right to enter onto the property for maintenance purposes.

5. PG&E has agreed to participate in a clean-up project implemented by the California Department of Toxic Substances Control. PG&E has commenced remediation of the property, and will leave $1.5 million in escrow upon the sale of the property to complete the remediation work.

6. The gain on sale of the property is $16,310,641 before taxes and $9,664,707 after taxes.

7. The City Council of the City of Union City is the Lead Agency for the proposed project under CEQA.

8. The City Council prepared an EIR for the project, which found that (a) the proposed project, the mitigation measures applicable to the project, and the Mitigation Monitoring Program avoids and/or reduces the majority of potential environmental impacts of the project to less-than-significant levels; (b) there is

substantial evidence in the record that each of the identified alternatives is infeasible because they would not allow the project to achieve its basic objectives nor accomplish the goals and policies of the City Council Redevelopment Plan and other adopted City Council policies; (c) certain mitigation measures as described in the FEIR would lessen but not necessarily eliminate the potential adverse environmental effect associated with the project and that those impacts in the areas of Air Quality, Noise, Traffic, and Circulation remain significant and unavoidable; and (d) there were no other feasible mitigation measures or alternatives which would reduce these impacts to less-than-significant levels.

9. On March 12, 2002, the City Council exercised its discretionary authority and subsequently adopted the FEIR, including applicable Mitigation Measures, the Mitigation Monitoring and Reporting Program, and a Statement of Overriding Considerations (Resolution No. 249-02, Exhibit A).

10. The California Public Utilities Commission (CPUC) is a Responsible Agency for the proposed project under CEQA.

11. Consistent with the City Council's findings and determinations, we find that, (a) the proposed project, the mitigation measures applicable to the project, and the Mitigation Monitoring Program avoids and/or reduces the majority of potential environmental impacts of the project to less-than-significant levels; (b) there is substantial evidence in the record that each of the identified alternatives is infeasible because they would not allow the project to achieve its basic objectives nor accomplish the goals and policies of the City Council's redevelopment plans and other adopted regional policies; (c) certain mitigation measures as described in the FEIR would lessen but not necessarily eliminate the potential adverse environmental effects associated with the project; (d) impacts in the areas of Air Quality, Noise, Traffic, and Circulation remain significant and

unavoidable; and (e) there were no other feasible mitigation measures or alternatives which would reduce these impacts to less-than-significant levels.

12. The property at issue is in rate base.

13. Investment in the land at issue was not a risky investment for shareholders.

14. Ratepayers contributed capital to the purchase of the property at issue.

15. The property was used to perform functions related to the regulated portion of PG&E's business.

Conclusions of Law

1. We should grant PG&E's application pursuant to Pub. Util. Code § 851 to sell a parcel of land to Union City, California.

2. The proposed agreement does not impair PG&E's ability to provide utility service to the public and provides positive public benefits.

3. The property at issue is no longer used by or useful to PG&E.

4. The EIR and the discretionary Decision by the City Council are adequate for the CPUC's decision-making purposes as a Responsible Agency under CEQA.

5. We should adopt the City Council's Mitigation Monitoring Program and Statement of Overriding Considerations for purposes of our approval.

6. Ratepayers and shareholders should share 50-50 in the gain on sale of the property.

7. This decision is based on the facts of this case and does not establish a general rule for allocation of the gain on sale in land sale cases. It may be that other, similar cases arise before we open our generic rulemaking. Those cases should be determined on their merits, without reliance on this decision, so that

we can leave establishment of a general, precedential rule to our upcoming gain on sale rulemaking.

O R D E R

IT IS ORDERED that:

1. We grant Pacific Gas and Electric Company's (PG&E) application pursuant to Pub. Util. Code § 851 to sell a parcel of land to the Community Redevelopment Agency of the City of Union City (Union City), California identified by the Alameda County Assessor as Assessor's Parcel Map 087-0019-004-02.

2. We adopt the City Council of Union City's Mitigation Monitoring Program and Statement of Overriding Considerations for purposes of our approval.

3. PG&E shall allocate the gain on sale from the property 50-50 between its shareholders and ratepayers, and make a compliance filing with the Commission within 30 days of the effective date of this decision indicating that it has complied with this mandate.

4. This proceeding may not be relied upon as precedent.

5. This proceeding is closed.

This order is effective today.

Dated _____, at San Francisco, California.